

AUDITORS' REPORT

To the Shareholders of
Opal Energy Inc.

We have audited the balance sheet of Opal Energy Inc. as at December 31, 1994 and the statement of income and equity and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. These standards require that we plan and perform the audit to obtain reasonable assurance whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. It also includes assessing the accounting principles used and significant estimates made by management.

OPAL ENERGY INC.
1994 FINANCIAL STATEMENTS

In our opinion, these financial statements present fairly, in all material aspects, the financial position of the Company as at December 31, 1994 and 1993 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles.

Ernst & Young
February 23, 1995

Ernst & Young
Chartered Accountants

AUDITORS' REPORT

To the Shareholders of
Opal Energy Inc.

We have audited the balance sheets of Opal Energy Inc. as at December 31, 1994 and 1993 and the statements of income and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.


We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1994 and 1993 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles.

Calgary, Canada
February 23, 1995

Ernst & Young

Chartered Accountants



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Opal Energy Inc.

BALANCE SHEETS

As at December 31

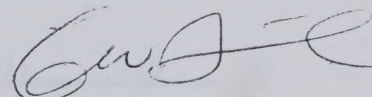
| | 1994 \$ | 1993 \$ |
|---|----------------|----------------|
| ASSETS | | |
| Current | | |
| Cash and short term deposits | 310,507 | 25,015 |
| Accounts receivable | 7,794 | 20,660 |
| Prepaid expense | 13,450 | 3,371 |
| | <u>331,751</u> | <u>49,046</u> |
| Capital assets [notes 2 & 4] | <u>485,725</u> | <u>522,665</u> |
| | <u>817,476</u> | <u>571,711</u> |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current | | |
| Accounts payable | 101,489 | 50,391 |
| Note payable [notes 3 & 9] | 18,750 | 18,750 |
| | <u>120,239</u> | <u>69,141</u> |
| Convertible debenture [note 4] | <u>200,000</u> | <u>200,000</u> |
| Commitments and contingencies [note 9] | | |
| SHAREHOLDERS' EQUITY | | |
| Share capital [note 5] | 685,966 | 479,204 |
| Deficit | (188,729) | (176,634) |
| | <u>497,237</u> | <u>302,570</u> |
| | <u>817,476</u> | <u>571,711</u> |

See accompanying notes

On behalf of the Board:

J.S. Duante

Director



Director

Opal Energy Inc.

STATEMENTS OF INCOME AND DEFICIT

For the years ended December 31

| | 1994 \$ | 1993 \$ |
|--|------------------|------------------|
| Revenue | | |
| Production income, net of royalties | 3,910 | 51,170 |
| Interest income | 12,538 | 335 |
| | <u>16,448</u> | <u>51,505</u> |
| Expenses | | |
| Production | 204 | 13,606 |
| General and administration | 45,375 | 33,052 |
| Depletion, depreciation and site restoration | 2,132 | 20,227 |
| Debt interest | 20,005 | — |
| Professional fees | 19,997 | 25,470 |
| | <u>87,713</u> | <u>92,355</u> |
| Loss from operations | (71,265) | (40,850) |
| Gain on disposal of resource properties [note 2] | <u>59,170</u> | <u>—</u> |
| Loss before income taxes and extraordinary item | (12,095) | (40,850) |
| Income taxes [note 6] | <u>—</u> | <u>—</u> |
| Loss before extraordinary item | (12,095) | (40,850) |
| Extraordinary item [note 7] | | |
| Gain on forgiveness of amounts payable to certain shareholders | <u>—</u> | <u>106,000</u> |
| Net income (loss) for the year | (12,095) | 65,150 |
| Deficit, beginning of the year | <u>(176,634)</u> | <u>(241,784)</u> |
| Deficit, end of the year | <u>(188,729)</u> | <u>(176,634)</u> |
| Loss per share - before extraordinary item [note 8] | <u>(0.01)</u> | <u>(0.01)</u> |
| Net income (loss) per share - after extraordinary item [note 8] | <u>(0.01)</u> | <u>0.02</u> |

See accompanying notes

Opal Energy Inc.

STATEMENTS OF CASH FLOWS

For the years ended December 31

| | 1994 \$ | 1993 \$ |
|--|-----------------|------------------|
| Cash provided by (used in) operating activities | | |
| Loss before extraordinary item | (12,095) | (40,850) |
| Add (deduct) charges to income not requiring a current cash payment | | |
| Depletion, depreciation and site restoration | 2,132 | 20,227 |
| Gain on disposal of resource properties | (59,170) | — |
| Cash flow from operations | (69,133) | (20,623) |
| Net change in non-cash working capital related to operations | (14,974) | 31,253 |
| | <u>(84,107)</u> | <u>10,630</u> |
| Cash provided by (used in) financing activities | | |
| Issuance of convertible debenture | — | 200,000 |
| Issuance of shares, net of share issue costs | 263,200 | 357,000 |
| | <u>263,200</u> | <u>557,000</u> |
| Cash provided by (used in) investing activities | | |
| Acquisition of capital assets | (537,186) | (542,806) |
| Proceeds from disposal of capital assets | 574,554 | — |
| Net change in non-cash working capital related to investing activities | 69,031 | — |
| | <u>106,399</u> | <u>(542,806)</u> |
| Change in cash during the year | 285,492 | 24,824 |
| Cash and short term deposits, beginning of the year | 25,015 | 191 |
| Cash and short term deposits, end of the year | 310,507 | 25,015 |
| Cash flow from operations per share [note 8] | (.01) | (.01) |

See accompanying notes

Opal Energy Inc.

NOTES TO FINANCIAL STATEMENTS

December 31, 1994

Opal Energy Inc. (formerly Westaurum Copper Corporation) is a public company incorporated under the Canada Business Corporation Act. Pursuant to an agreement dated August 27, 1993 new shareholders acquired a substantial number of shares of the Company. Prior to this acquisition, the Company was inactive. The Company resumed activity as of August 27, 1993 under new management and a new Board of Directors. The name of the Company was changed from Westaurum Copper Corporation to Opal Energy Inc. on October 14, 1993.

The financial statements of the Company have been prepared in accordance with generally accepted accounting principles. The financial statements, in management's opinion, have been properly prepared within reasonable limits of materiality and within the framework of accounting policies summarized below.

1. SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The accompanying financial statements have been prepared on a going concern basis which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. The Company is in the development stage exploring for oil and gas reserves. The ability of the Company to continue as a going concern is dependent on obtaining additional financing and discovering proven reserves.

These financial statements do not include any adjustments to the amounts and classification of assets and liabilities that may be necessary should the Company become unable to continue as a going concern.

Petroleum and natural gas properties

The Company follows the full cost method of accounting for its petroleum and natural gas properties. All costs related to the exploration for and development of petroleum and natural gas reserves, whether productive or non-productive, are capitalized in one Canadian cost centre and charged against earnings as set out below. Such costs include land acquisition, drilling, geological and geophysical costs, lease rentals on undeveloped properties and drilling costs of both productive and non-productive wells.

Gains or losses are not recognized upon disposition of petroleum and natural gas properties unless crediting the proceeds against accumulated costs would result in a change in the rate of depletion of 20% or more as a result of the disposition.

Depletion is provided using the unit of production method based on proven petroleum and natural gas reserves before royalties as determined by independent consulting engineers. For the purpose of this calculation, reserves and production of oil and natural gas liquids are converted to equivalent units of oil based on relative energy content.

Opal Energy Inc.

NOTES TO FINANCIAL STATEMENTS

December 31, 1994

The estimated cost of site restoration is based on the current cost and the anticipated method and extent of site restoration in accordance with existing legislation and industry practice. Estimated future site restoration costs are accrued on a unit of production basis based on proven reserves. The provision is recorded on the statement of operations as depletion and depreciation and on the balance sheet as a long term liability. Where expenditures are made to restore a property, the accumulated provision is charged with these expenditures. There was no commercial production from the petroleum and natural gas properties during fiscal 1994, therefore no provision for site restoration was recorded in the accounts.

The carrying value of the Company's petroleum and natural gas properties, net of deferred income taxes and site restoration provision is limited to an ultimate recoverable amount. This amount is the aggregate of estimated future net revenues from proved reserves and the costs of unproved properties, net of impairment allowances, less future estimated production general and administrative costs, financing costs, the estimate of future site restoration costs, net of salvage values, and income taxes. Future net revenues are estimated using year end prices and costs without escalation or discounting and the income tax and Alberta royalty tax credit legislation in effect at the year end.

Depreciation of production equipment and facilities is computed on the unit-of-production method based on estimated proven petroleum and natural gas reserves. Depreciation of furniture and fixtures is provided for on a declining basis at an annual rate of 20%. Depreciation of computers is provided for on a declining basis at an annual rate of 30%.

Income taxes

The Company follows the tax allocation method of accounting under which the income tax provision is based on the earnings reported in the accounts. Under this method, the Company provides for deferred income taxes to the extent that income taxes otherwise payable are reduced by capital cost allowances and exploration and development costs in excess of the depreciation and depletion and amortization provisions recorded in the accounts.

Joint venture accounting

All of the exploration and production activities of the Company are conducted jointly with others and accordingly these financial statements reflect only the Company's proportionate interest in such activities.

Flow through shares

Flow through common shares are initially recorded at net proceeds. Share capital and capital assets are reduced by the tax effect of the expenditures renounced to the shareholders as the expenditures are incurred.

Opal Energy Inc.

NOTES TO FINANCIAL STATEMENTS

December 31, 1994

2. CAPITAL ASSETS

| | 1994 | | |
|--------------------------------------|----------------|--|-------------------|
| | Cost | Accumulated Depletion and Depreciation | Net Book Value |
| | \$ | \$ | \$ |
| Petroleum and natural gas properties | 475,277 | — | 475,277 |
| Computer | 2,953 | 992 | 1,961 |
| Furniture & fixtures | 10,642 | 2,155 | 8,487 |
| | <u>488,872</u> | <u>3,147</u> | <u>485,725</u> |

| | 1993 | | |
|--------------------------------------|----------------|--|-------------------|
| | Cost | Accumulated Depletion and Depreciation | Net Book Value |
| | \$ | \$ | \$ |
| Petroleum and natural gas properties | 534,596 | 19,212 | 515,384 |
| Computer | 2,150 | 323 | 1,827 |
| Furniture & fixtures | 6,060 | 606 | 5,454 |
| | <u>542,806</u> | <u>20,141</u> | <u>522,665</u> |

During the first quarter of 1994 the Company sold two of its natural gas properties for net proceeds of \$574,554. These properties represented substantially all of the producing petroleum and natural gas properties of the Company, and accordingly, a gain on disposal of \$59,170 was recognized.

During the year, \$64,884 (1993 - \$nil) of general and administration expenses were capitalized.

All petroleum and natural gas properties at December 31, 1994 are unproven, and are excluded from the depletion calculation.

3. NOTE PAYABLE

The note payable is unsecured, non interest bearing with no fixed terms of repayment (note 9).

Opal Energy Inc.

NOTES TO FINANCIAL STATEMENTS

December 31, 1994

4. CONVERTIBLE DEBENTURE

The Company has a \$200,000 10% convertible debenture due September 9, 1996 with interest due monthly. The debenture is convertible into common shares of the Company at a conversion price of \$1.00 per common share and can be converted at any time up to the maturity date. The petroleum and natural gas properties of the Company are pledged as collateral for the debenture.

5. SHARE CAPITAL

Authorized

Unlimited number of common shares
Unlimited number of preferred shares

Issued

Common shares issued and outstanding are as follows:

| | Number of Shares | Consideration \$ |
|---|---------------------|---------------------|
| Outstanding at December 31, 1992 | 1,803,750 | 122,204 |
| Issued pursuant to August 27, 1993 private placement for cash | 2,500,000 | 92,500 |
| Issued pursuant to September 9, 1993 private placement for cash | 1,078,000 | 269,500 |
| Share issue costs | — | (5,000) |
| Outstanding at December 31, 1993 | 5,381,750 | 479,204 |
| Issued pursuant to July 11, 1994 private placement for cash | 52,800 | 13,200 |
| Flow through shares issued pursuant to subscription agreements dated September 1, 1994 | 714,288 | 250,000 |
| Tax benefit related to qualified expenditures renounced to subscribers of flow through common shares | — | (56,438) |
| Outstanding at December 31, 1994 | 6,148,838 | 685,966 |

Opal Energy Inc.

NOTES TO FINANCIAL STATEMENTS

December 31, 1994

On August 27, 1993 the Company completed a private placement of 2,500,000 shares at an issue price of \$0.037. The proceeds of \$92,500 were used to finance the acquisition of petroleum and natural gas properties.

On September 9, 1993 the Company completed a private placement of 1,078,000 shares at an issue price of \$0.25 per share. The proceeds of \$269,500 were used to finance the acquisition of petroleum and natural gas properties.

On July 11, 1994 the Company issued 52,800 shares to an employee for gross proceeds of \$13,200.

On September 1, 1994 the Company issued 714,288 flow through shares for gross proceeds of \$250,000 which require the Company to renounce \$250,000 of its expenditures on oil and gas properties. At December 31, 1994 \$128,269 qualified expenditures had been renounced, decreasing the value of share capital and resource properties by \$56,438.

Options and Warrants

During the year, the Board of Directors approved the granting of options to certain directors, officers and employees to purchase the Company's common shares. At December 31, 1994, the Company has reserved and stock options have been issued for a total of 495,500 shares at an exercise price of \$0.25 per share. The options expire at various dates up to April 28, 1999.

The Company issued 357,144 warrants which entitles the holders to acquire one common share at \$0.50 on or before September 1, 1995.

6. INCOME TAXES

The provision for deferred taxes is different from the amount computed by applying the statutory rate of 44.34% to the loss before income taxes and extraordinary item. The reasons for these differences are as follows:

| | 1994 | 1993 |
|---|-------------------|-------------------|
| Loss before income taxes and extraordinary item | \$12,095 | \$40,850 |
| Corporate income tax rate | 44.34 % | 44.34% |
| Expected provision for income taxes | \$ (5,363) | \$(18,113) |
| Increase (decrease) in taxes resulting from: | | |
| Resource allowance, net of non-deductible depletion | — | (2,912) |
| Unrecognized losses for accounting purposes | 5,363 | 21,468 |
| Other | — | (443) |
| Deferred income taxes | — | — |

Opal Energy Inc.

NOTES TO FINANCIAL STATEMENTS

December 31, 1994

At December 31, 1994 the Company has losses carried forward for tax purposes aggregating approximately \$129,000 (1993 - \$65,700) expiring as follows:

| | |
|------|------------------|
| 1999 | \$ 37,500 |
| 2000 | 19,800 |
| 2001 | <u>71,700</u> |
| | <u>\$129,000</u> |

No recognition has been given in these financial statements to any potential tax savings which may result from these losses carried forward.

7. EXTRAORDINARY ITEM

During 1993, a total of \$106,000 of amounts payable by the Company to certain shareholders was forgiven. This forgiveness of debt results in a reduction of losses carried forward for tax purposes of \$106,000.

8. EARNINGS AND CASH FLOW FROM OPERATIONS PER SHARE

Earnings and cash flow from operations per share have been calculated based on the weighted average number of shares outstanding for the year ended December 31, 1994 of 5,645,524 (1993 - 3,010,303).

Cash flow from operations per share has been calculated based on cash flow from operations before the net change in non-cash working capital related to operations.

Fully diluted earnings and cash flow from operations per share have not been presented because there is no material difference from basic earnings and cash flow from operations per share.

9. COMMITMENTS AND CONTINGENCIES

The Company has an operating lease commitment for office space through December 31, 1995. The minimum payments under this lease are approximately \$19,000.

In 1994 the Company discontinued payment on the note payable as a result of a dispute regarding the terms and consideration on the purchase of the properties. On January 27, 1994, a Statement of Claim was filed against the Company for the amount owing under the note. The Company is of the view that these funds are no longer owing and have counterclaimed for \$6,785 representing funds paid on the note payable net of adjustments. Management and its legal counsel are of the opinion that the Company is in a solid position to defend this claim.

